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MICHAEL R. HAVERTY
CHAIRMAN, PRESIDENT AND
CHIEF EXECUTIVE OFFICER

June 28, 2004

Chairman Roger Nober
Surface Transportation Board
1925 K Street NW, Suite 810
Washington, DC 20433

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BOARD
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OFFICE OF CHAIRMAN
NOBER

Dear Chairman Nober,

Thank you for your letter concerning the KCS's view of fall peak demand, our plan to meet that demand and our approach to communicating that plan to our customers.

While we know that the Board closely monitors our performance metrics, I would like to begin by pointing out that KCS's performance has improved continuously over the past year and that KCS is at or near the best performance level of the Class I railroads in each of the reported categories. This improved operating performance occurred even though we have experienced very strong traffic growth (more than 6% growth over the same period last year). Our metrics show that KCS has been effective in delivering committed service levels to customers while we handle their increased volumes.

We maintain close contact with our customers for a host of reasons, including gaining real time updates about demand. Based upon our customers' input along with that of our connections, including our shortline partners, and available forecasts of the U.S., North American and World economic activity, the outlook for most of our commodities is for four to five percent year-over-year growth during this year's peak period. Intermodal growth, however, is expected to be much stronger – in the range of 12-15 percent.

Our service goals for the next 120 days are to maintain our current high level of service with the potential for delivering a slight improvement. The elements of our plan to effectively service our customers have not changed recently, but reflect our objective of continuous improvement.

Tightly managing our operations is key to our service delivery plan. With the implementation of our MCS operating system, our managers have accurate and timely information to support their decision making in order to deliver the service sold to the customer but within a tight cost envelope. It is our people who are responsible for delivering the higher quality service.

We also have added capacity to our system since the first of 2004. We have:

- Acquired 52 locomotives (36 purchased and 16 leased) which represents an 11% increase in our road fleet; and have rebuilt 15 locomotives that were heavy bad order which, in total, represents a 14% increase in our available road locomotive fleet.
- Improved locomotive maintenance by implementing a number of enhancements, including condition-based maintenance.
- Standardized tools and procedures to improve the quality of locomotive and car repairs and the productivity of our employees.
- Initiated a program to monitor locomotive location, and crew and locomotive performance levels by equipping 37 locomotives with a complete GPS-based electronic monitoring package.
- Increased the availability and effectiveness of our End of Train (EOT) devices by:
 - increasing the number of radio repeaters to eliminate dead spots;
 - expanding the use of EOT pretest systems to reduce initial terminal delays;
 - beginning to take delivery of self powered EOT's (which eliminates battery-related failures and the associated train delays).
- Increased our line capacity on our fastest growing Meridian-Alliance route by:
 - adding three new sidings, with two more to be completed late this year or early next year;
 - making changes that allowed increased operating speed on 20% of the Meridian-Alliance route;
 - completing all maintenance on this route before the start of peak season.
- Rebuilt the switching leads and switches at Shreveport, to facilitate the flow of traffic through this hub yard.
- Increased the number and improved the training of our employees.
 - Added to the carmen force and redistributed those employees for maximum impact.
 - Hired mechanics to handle the increased fleet, to expedite repairs and to reduce reliance on third party providers.
 - Hired more conductors in the first six months of 2004 than in all of 2003, and our current rate of hiring will continue through the remainder of the year with the result that our hiring will be more than double that of last year.
 - All mechanical employees will receive at least 40 hours of training and a management training program has been launched for all mechanical supervisors.

While there are other initiatives that could be listed, our service performance demonstrates that we have been effective in meeting our customers' requirements.

While KCS's plans have been successful in maintaining service metrics, we have had to make adjustments to reflect the service disabilities of some of the other Class I railroads. For example, those service problems have greatly slowed the return of empty cars which has led to tight car supply and loss of loadings at, for example, paper shippers. To mitigate the impact of this slow return, we very tightly manage the flow of both loaded and empty cars, and we often make special moves to ensure that shippers have adequate car supply.

The velocity of cars across the system is critical. In 2003, KCS increased its car velocity 25% over 2002 and in 2004, we have been able to hold the higher velocity. For our grain customers, this increased velocity together with the limited success we have had in adding to our car fleet has yielded a nearly 30% increase in our grain handling ability. We will take delivery of 76 high capacity (5150 cubic foot) grain hopper cars which we will put in quick turn shuttle service in order to effectively and efficiently handle our on-line grain shippers volume during the fall harvest.

Perhaps the most significant impact of the service problem faced by Union Pacific has been felt on the Tex Mex which, as you know, is owned in part by KCS. The Tex Mex operates under trackage rights over some 350 miles between Beaumont and Robstown, Texas over the UP. These trackage rights are necessary for Tex Mex to fulfill its role as a competitor to UP for Mexico traffic over the Laredo gateway. Traffic growth on both the Tex Mex and the UP has been met with inadequate maintenance and capacity investment by UP with the result that transit time is now double what was committed to by the UP when the Surface Transportation Board granted the trackage rights to Tex Mex in 1996. Because of UP's failure to maintain adequate capacity, shippers are being adversely impacted in both the U.S. and in Mexico. In addition, costs on the Tex Mex are being forced up as it hires more people, undertakes more investment in roadway, cars and locomotives all with limited success in offsetting the basic effects of congestion on the trackage rights over the UP.

Communication of our plans and actions to KCS's customers is constant and utilizes multiple channels. Our account managers along with our Account Management and Customer Service Centers are the primary method of communication and they are in constant two-way communication with our customers. These communications move forward on two levels – plans and programs, and transactions. As examples of our communication to customers on the issues you have raised, Attachments I and II are Performance and Progress Reports which our Account Managers delivered to customers in January and in March of this year.

In addition, KCS communicates with its customers at trade association meetings (such as National Feed and Grain, and National Freight Transportation Association), rail shipper association meetings (NARS, SWARS, SEARS Midwest, NEAR, PNWARS) and special meetings such as the customer meeting to be held in Kansas City on September 9.

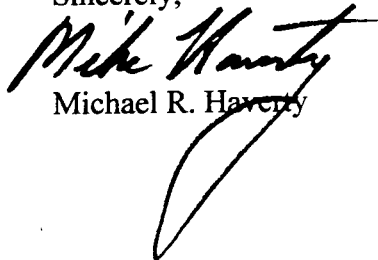
We also communicate using our website (four examples are contained in Attachment III); KCS News (which is published weekly and is distributed to customers, employees and others and included in our website is shown in Attachment IV); regular customer communications, called Connections (two examples are contained in Attachment V); and through special presentations to customers.

In summary, KCS has been effective at satisfying the objectives of meeting the customers' service requirements, accomplishing the right capacity-expanding investments at the right time and keeping our costs under control.

We at KCS are looking forward to serving the increased volumes during the peak season. I am confident that we do so while delivering service metrics that are at the leading edge of the industry.

Of course, I am prepared to discuss any aspect of this brief summary at the convenience of the Board.

Sincerely,

A handwritten signature in black ink, appearing to read "Mike Haverly", with a large, stylized flourish extending from the bottom right.

Michael R. Haverly

cc: The Honorable W. Douglas Buttrey
The Honorable Francis Mulvey
Ms. Betty Monroe, Acting Administrator, Federal Railroad Administration
Edward R. Hamberger, President, Association of American Railroads